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No. 90-1965

In The

Supreme Court of the United States

October Term, 1991

BORMAN'S, INC.,

Petitioner,

v.

MICHIGAN PROPERTY & CASUALTY GUARANTY ASSOCIATION,

Respondent.

Petition For Writ Of Certiorari To The United States Court Of Appeals For The Sixth Circuit

BRIEF OF THE MICHIGAN PROPERTY & CASUALTY GUARANTY ASSOCIATION IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI

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COUNTERSTATEMENT OF THE QUESTIONS PRESENTED

In 1969, the Michigan legislature enacted a statute creating the Michigan Property & Casualty Guaranty Association. The Association was created to pay certain, but not all, obligations (called "covered claims") of insolvent property/casualty insurers to their Michigan insureds and to persons with claims against Michigan insureds. Recognizing that it was appropriate, given the limited resources available to the Association, to restrict the payment of claims to those asserted by persons least able financially to absorb an unexpected and uninsured loss, the legislature enacted a provision in the 1969 statute excluding from the definition of a "covered claim" "obligations to . . . a person who has a net worth greater than 1/10 of 1% of the aggregate premiums written by member insurers" in Michigan in the calendar year preceding insolvency.

In this challenge to the "net worth" provision under the Equal Protection Clause of the United States Constitution, the questions presented are as follows:

> 1. Where the district court characterized its conclusion on the constitutional issue as a "finding" but did not determine any disputed issues of fact and where, in any event, the court of appeals accepted the factual record developed in the district court, was the court of appeals bound by Fed. R. Civ. P. 52(a) to accept the district court's conclusion that there is no rational relationship between a person's net worth and his or her relative ability to absorb an uninsured loss?

COUNTERSTATEMENT OF THE QUESTIONS PRESENTED – Continued

2. Did the court of appeals correctly hold – given the admittedly conflicting evidence on the question whether there is a rational relationship between net worth and the relative ability to absorb an uninsured loss – that the net worth provision is constitutional and that the district court improperly substituted its judgment for that of the legislature in concluding otherwise?

LIST OF PARTIES AND RULE 29.1 STATEMENT

The parties to the proceedings below were Petitioner and Respondent.

The Petitioner is Borman's, Inc. ("Borman's"). Borman's is a wholly owned subsidiary of The Great Atlantic & Pacific Tea Company, Inc. At the time of trial, Borman's was a public company. It became a wholly owned subsidiary in February, 1989.

The Respondent is the Michigan Property & Casualty Guaranty Association (the "Association"). The Association is not a subsidiary or affiliate of any publicly owned corporation. By law, however, every property/casualty insurer authorized to transact insurance in Michigan, one or more of whom may be publicly owned companies or subsidiaries or affiliates of publicly owned companies, is a member of the Association.

TABLE OF CONTENTS

Page

COUNTERSTATEMENT OF THE QUESTIONS PRESENTED i

LIST OF PARTIES AND RULE 29.1 STATEMENT... iii

TABLE OF CONTENTS iv

TABLE OF AUTHORITIES vi

COUNTERSTATEMENT OF THE CASE 1

1. Description Of The Association And Of The Legislation Before The Court 1

2. Facts Giving Rise To This Lawsuit 4

3. Course Of This Litigation Below 5

SUMMARY OF ARGUMENT 9

ARGUMENT 11

I. THE COURT OF APPEALS' DECISION DOES NOT CONFLICT WITH THIS COURT'S DECISIONS CONCERNING FED. R. CIV. P. 52(a) BECAUSE RULE 52(a) DOES NOT APPLY TO THIS CASE, AS THE COURT OF APPEALS REVIEWED AND REVERSED ONLY THE DISTRICT COURT'S LEGAL CONCLUSION ON THE RELEVANT CONSTITUTIONAL QUESTION 11

II. THERE IS NO BASIS FOR GRANTING CERTIORARI IN THIS CASE BECAUSE THE COURT OF APPEALS CORRECTLY APPLIED THE SCOPE OF REVIEW REQUIRED BY THIS COURT IN RATIONAL BASIS CASES 16

TABLE OF CONTENTS – Continued

Page

A. Under The Rational Basis Test, The District Court Was Not Permitted To Weigh The Admittedly Conflicting Testimony Concerning The Efficacy And Wisdom Of The Legislature's Choices 17

B. Credible Evidence Of The History And Structure Of The Act, And The Testimony Of Qualified Experts In Accounting, Insurance And Insurance Regulation Support Its Rationality 22

CONCLUSION 30

TABLE OF AUTHORITIES

Page

CASES:

Baker v. Vanderbilt Univ., 616 F. Supp. 330 (M.D. Tenn. 1985) 7

Borden's Farm Prods. Co. v. Baldwin, 293 U.S. 194 (1934) 19, 20, 21

Bose Corp. v. Consumers Union of United States, Inc., 466 U.S. 485 (1984) 11, 12, 14, 15

Dandridge v. Williams, 397 U.S. 471 (1970) 19

McGowan v. Maryland, 366 U.S. 420 (1961) 7

Miller v. Fenton, 474 U.S. 104 (1985) 12, 13

Minnesota v. Cloverleaf Creamery Co., 449 U.S. 456 (1981) 12, 17, 18

Pullman-Standard v. Swint, 456 U.S. 273 (1982) 11

Salve Regina College v. Russell, ___ U.S. ___, 111 S.Ct. 1217 (1991) 12, 13

United States R.R. Retirement Bd. v. Fritz, 449 U.S. 166 (1980) 19

Vance v. Bradley, 440 U.S. 93 (1979) 19

STATUTES:

Mich. Comp. Laws Ann. § 500.7901-§ 500.7949 (West 1983 & Supp. 1991) 1

Mich. Comp. Laws Ann. § 500.7911 (West Supp. 1991) 2, 3

Mich. Comp. Laws Ann. § 500.7925 (West 1983) 3

TABLE OF AUTHORITIES – Continued

Page

Mich. Comp. Laws Ann. § 500.7925(3) (West 1983)..*passim*

Mich. Comp. Laws Ann. § 500.7931 (West 1983)....2, 3

Mich. Comp. Laws Ann. § 500.7941 (West Supp. 1991)..... 2

OTHER AUTHORITIES:

Fed. R. Civ. P. 52(a) 8, 10, 11, 13, 15

Sup. Ct. R. 10.1 9

COUNTERSTATEMENT OF THE CASE

In this rational basis equal protection case, the United States Court of Appeals for the Sixth Circuit held that under the applicable legal standard, the district court should have found as a matter of law that a statutory provision limiting entitlement to certain benefits on the basis of net worth did not violate the Fourteenth Amendment to the United States Constitution. The court of appeals, reviewing the same evidence considered by the district court, concluded that the Michigan legislature rationally could have believed that net worth is a reasonable indicator of a person's relative ability to absorb an unexpected loss occasioned by the insolvency of his or her insurer. Because the district court exceeded its authority in applying the pertinent equal protection test to the legislation before it, the court of appeals reversed and entered judgment in favor of the Respondent Michigan Property & Casualty Guaranty Association (the "Association"). By its Petition for a writ of certiorari, Borman's, Inc. ("Borman's") has asked this Court to review the court of appeals' holding that the district court misapplied the law.

1. Description Of The Association And Of The Legislation Before The Court

The Association is an entity created in 1969 when the Michigan legislature enacted the Property & Casualty Guaranty Association Act (the "Act"), codified in Chapter 79 of the Michigan Insurance Code of 1956, as amended, Mich. Comp. Laws Ann. § 500.7901-§ 500.7949 (West 1983 & Supp. 1991). It is an unincorporated association of

which every insurer (other than insurers transacting only life or disability insurance and certain statutorily-created insurers and insurance funds) must be a member as a condition of its authority to transact insurance in Michigan. *Id.*, § 500.7911 (West Supp. 1991). The Association pays certain policy obligations (called "covered claims") of property/casualty insurers that have been liquidated in receivership proceedings. *Id.*, § 500.7931(1) (West 1983).

The Association funds the payment of covered claims and its administrative expenses through assessments on solvent member insurers. *Id.*, § 500.7941 (West Supp. 1991). Covered claims paid by the Association are allocated to one of five categories: (1) worker's compensation insurance; (2) automobile insurance; (3) title insurance; (4) fire, allied lines, farm owner's multiple peril, homeowner's multiple peril, inland marine, earthquake and credit insurance and (5) all other kinds of insurance except life and disability. The Association is required to assess its members separately for each of these categories, and the assessment for one category may not be used to pay covered claims or related expenses in another category. *Ibid.* The Act limits annual assessments to one percent of the member's net direct premiums written in Michigan during the previous calendar year (*Ibid.*), thus limiting the resources available to the Association for the payment of covered claims.

The 1969 Act provides extensive, although not total, protection for Michigan insureds of insolvent property/casualty insurers and for persons with claims against these insureds. Indeed, consistent with the limited resources available to the Association, the Act reflects a number of public policy-oriented choices which have the

effect of providing full protection to some, incomplete protection to others and none to others still.

For example, the Act includes protection for all lines of property and casualty insurance, including financial guaranty insurance, credit insurance and other lines (*Id.*, § 500.7911), while many other states' guaranty funds do not provide such protection. Additionally, section 7925 of the Act, which defines the "covered claims" the Association is required to discharge, excludes claims for attorney fees, adjustment costs and interest incurred before an insurer's insolvency; excludes claims for unearned premium in excess of $500 (adjusted annually to account for changes in the consumer price index); excludes claims filed after the last date for the filing of claims in the receivership proceedings in the insolvent insurer's domiciliary state; excludes claims of other insurance companies, insurance pools and underwriting associations and excludes claims against the insurer that arise out of an unfair trade practice. *Id.*, § 500.7925 (West 1983). Additionally, section 7925 of the Act limits the total amount of a covered claim in any given year to 1/20 of one percent of the aggregate premiums written by member insurers during the calendar year preceding insolvency (compared with much lower limits in other states), although the Act sets no upper limit on the size of covered worker's compensation claims. *Ibid.* Another example of a policy choice which the legislature made in the Act is found in a collateral source rule that requires the Association to set off benefits or damages recoverable from another source of insurance as a credit against a covered claim (*Id.*, § 500.7931 (West 1983)).

The statutory provision challenged by Petitioner and upheld by the court of appeals – section 7925(3) of the Act – excludes from coverage under the Act obligations of an insolvent insurer to a person whose net worth in the year of the insurer's insolvency exceeds 1/10 of one percent of the aggregate premiums written by Association members in the calendar year preceding the insolvency. *Id.*, § 500.7925(3) (West 1983).[1]

2. Facts Giving Rise To This Lawsuit

From May 1, 1980 through May 1, 1984, Petitioner, which owns among other entities the Farmer Jack supermarket chain, was insured under a general liability policy issued by Ideal Mutual Insurance Company ("Ideal Mutual"). Trial Transcript ("Tr."), 1/9/89, pp. 41-42. Ideal Mutual insured Petitioner for losses up to $1 million in excess of a $50,000 self-insured retention. *Id.*, p. 43.

On August 7, 1980, during the period covered by the Ideal Mutual policy, Norris Frye was injured while shopping in a Farmer Jack supermarket. *Id.*, pp. 44-45. On August 7, 1981, Frye filed a complaint against Petitioner to recover damages for his injury. *Id.*, p. 62. On September 24, 1984, a Wayne County, Michigan jury awarded Frye $1.5 million. *Id.*, p. 45. Eventually Petitioner settled the

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[1] In 1984, the year prior to the insolvency involved in this case, property/casualty insurance writings in Michigan were approximately $4,696,500,000. Thus, the net worth "cutoff" in 1985 was $4,696,500. *Borman's, Inc. v. Michigan Property & Casualty Guaranty Ass'n*, 717 F. Supp. 480 (E.D. Mich. 1989), Appendix to Petition for writ of certiorari (hereafter "App."), p. A-25.

Frye case for $1.15 million. Under the terms of the general liability policy, Ideal Mutual was responsible for $950,000 of the settled-upon sum (its policy limits less Petitioner's self-insured retention). *Id.*, p. 47. Before Frye was paid, however, the New York Supreme Court ordered Ideal Mutual into rehabilitation on December 26, 1984, and enjoined further proceedings against the insurer. The New York court ordered Ideal Mutual liquidated on February 7, 1985. *Id.*, pp. 47-48. After the insolvency, Petitioner paid $1 million toward settlement of the *Frye* case. *Id.*, p. 53.

Petitioner sought payment from the Association of amounts paid to Frye and to several other persons whose claims would have been paid by Ideal Mutual had it remained solvent. Under the authority of section 7925(3), the Association denied coverage because Petitioner's net worth at the end of 1984, the year immediately preceding Ideal Mutual's insolvency, was nearly $24 million, exceeding the $4.7 million cutoff established for 1985 insolvencies by over $19 million. Petitioner's lawsuit arose from the Association's denial of its claims.

3. Course Of This Litigation Below

Petitioner filed this lawsuit for declaratory and monetary relief on January 9, 1986, challenging section 7925(3) under the Equal Protection and Due Process Clauses of the United States and Michigan Constitutions. On December 10, 1987, the district court denied the parties' cross-motion for summary judgment on the constitutional issues, but held that the applicable legal test against which the constitutionality of section 7925(3) is to be

measured is the "rational basis" standard. App., pp. A-40-A-41.

For seven days between January 9 and 24, 1989, the case was tried before United States District Judge Barbara K. Hackett without a jury. On June 30, 1989, the district court issued an opinion and judgment declaring that section 7925(3) of the Act violates Petitioner's equal protection rights under the federal and Michigan Constitutions. *Id.*, p. A-37. In addition, the district court ordered the Association to pay claims which Petitioner had to pay because of Ideal Mutual's insolvency. These claims total approximately $1.2 million. Order Amending Judgment And Opinion, *Id.*, pp. A-15-A-17.

The district court ordered that its judgment apply prospectively only. On July 31 and August 29, 1989, the court amended its judgment to clarify the prospective-application ruling. The court ordered that, except for the $1.2 million in claims noted above and other amounts payable under the Ideal Mutual policy for which Borman's filed a timely claim with the Association, its June 30, 1989 judgment would apply only to claims filed with the Association arising under policies issued by insurers which became insolvent after June 30, 1989.

The Association appealed the trial court's opinion and judgment to the United States Court of Appeals for the Sixth Circuit. In an opinion and by a judgment filed on February 7, 1991, the court of appeals reversed the district court. *Borman's, Inc. v. Michigan Property & Casualty Guaranty Ass'n*, 925 F.2d 160 (6th Cir. 1991). The court of appeals summarized the question before it and the

scope of its holding in the opening paragraph of its opinion:

> This appeal presents the question of whether the district court erred in finding that Mich. Comp. Laws § 500.7925(3), which excludes from coverage certain insureds whose net worth exceeds a statutorily-calculated maximum under the Michigan Property & Casualty Guaranty Act, is not rationally related to a legitimate governmental purpose in violation of the equal protection clause of the United States Constitution and the Michigan Constitution. As we find that the district court exceed its scope of review in assessing the constitutionality of § 500.7925(3), we reverse.

Id., pp. A-1-A-2.

After discussing the applicable equal protection standard (*Id.*, pp. A-4-A-5), which Petitioner and the Association agree applies to this review of socioeconomic legislation, the court of appeals stated the legal issue in this case in the following terms:

> Against this background, we must decide whether the Michigan legislature's determination that net worth was an appropriate means of predicting the ability of a company to absorb unexpected loss was so irrational that no state of facts 'reasonably may be conceived to justify it.'

Id., p. A-5 (quoting from *Baker v. Vanderbilt Univ.*, 616 F. Supp. 330, 331 (M.D. Tenn. 1985), which in turn quotes *McGowan v. Maryland*, 366 U.S. 420, 426 (1961)). The court of appeals held that "within this extremely narrow scope of review, the Michigan legislature's reliance on net worth in § 7925(3) passes constitutional muster." App., p. A-5.

The court of appeals discussed the evidence offered at trial, which the district court conceded was "conflicting," on the question whether net worth is a rational indicator of one's relative ability to absorb losses. *Id.*, p. A-36. Summarizing its discussion, the court of appeals held:

> [w]hile the Association did not by any means prove that net worth was the best mechanism for determining ability to absorb loss, it did put on sufficient evidence to suggest that factual circumstances were conceivable which justify the legislature's use of net worth as a proxy for a more complex calculation. Further, the Association put on evidence to suggest that the net worth standard was much easier to administer than more complex standards. While ease-of-administration, on its own, is not sufficient to justify an otherwise irrational legislative enactment, *United States Dep't of Agriculture v. Murry*, 413 U.S. 508, 513 (1973), it is beyond dispute that the legislature may consider the administrative difficulties of individual eligibility determinations in making 'a substantive policy determination that limited resources would not be well spent in making individual determinations.' *Weinberger v. Salfi*, 422 U.S. 749, 784 (1975).

Id., p. A-7.

On February 18, 1991, Petitioner filed a petition for rehearing and for rehearing *en banc*. This petition raised the same arguments which Borman's makes in its Petition to this Court for a writ of certiorari: (1) that the court of appeals violated Fed. R. Civ. P. 52(a) by failing to follow the district court's "factual findings" in the absence of a determination that such findings were clearly erroneous and (2) that the court of appeals erred in determining in

the face of conflicting evidence that Borman's had not satisfied its burden of overcoming the presumption of constitutionality attaching to section 7925(3).

In an Order filed on March 25, 1991, the court of appeals denied rehearing *en banc* and denied Borman's petition for rehearing. The court of appeals' February 7, 1991 judgment was thus issued as the court's mandate on April 3, 1991. The instant Petition for a writ of certiorari followed.

SUMMARY OF ARGUMENT

This Court's rules caution that "review on writ of certiorari is not a matter of right, but of judicial discretion. A petition for a writ of certiorari will be granted only when there are special and important reasons therefor." Sup. Ct. R. 10.1. Borman's Petition plainly fails to satisfy this threshhold requirement. It raises no constitutional questions of any import. Nor is there any issue in this case involving the construction or application of a federal statute. The court of appeals' decision does not conflict with a decision of another United States Court of Appeals (or with a decision of any other court, for that matter). Instead, in a rather unexceptional rational basis case, the court of appeals held that the district court misapplied the law and, contrary to this Court's decisions establishing a very limited scope of review in such cases, improperly substituted its own judgment for that of the Michigan legislature.

Although Petitioner attempts to cast its disagreement with the court of appeals' decision as one involving the

Sixth Circuit's "fail[ure] to give the required deference to the District Court's findings" of fact (Petition, p. 10), this case does not even remotely involve Fed. R. Civ. P. 52(a). The court of appeals reviewed the same testimony as the district court (none of which the district court found to lack credibility). The court of appeals did not "find" any facts. Instead, the court *accepted* the factual record developed before the district court and merely reviewed that record within the limits established by this Court's rational basis equal protection cases (that is, without *weighing* Petitioner's evidence against the Association's or reaching a judgment as to the relative wisdom of using net worth in the Act *vis a vis* a more complex measure of ability to absorb loss). Then, consistent with its statement of the purely legal issue before it, the court of appeals "decide[d] whether the Michigan legislature's determination that net worth was an appropriate means of predicting the ability of a company to absorb unexpected loss was so irrational that no state of facts 'reasonably may be conceived to justify it.' " App., p. A-5.

If this Court sanctions Petitioner's attempt to recast the district court's application of the equal protection test in this case as a "finding of fact," the federal appellate courts, including this one, effectively would be precluded from *ever* reviewing what plainly are a district court's conclusions of law any time the court chooses to call them "findings of fact." Notwithstanding Petitioner's linguistic sleight of hand, it is clear that the court of appeals decided a question of law, not fact, and thus did not exceed the scope of its permissible *de novo* appellate review.

ARGUMENT

I. THE COURT OF APPEALS' DECISION DOES NOT CONFLICT WITH THIS COURT'S DECISIONS CONCERNING FED. R. CIV. P. 52(a) BECAUSE RULE 52(A) DOES NOT APPLY TO THIS CASE, AS THE COURT OF APPEALS REVIEWED AND REVERSED ONLY THE DISTRICT COURT'S LEGAL CONCLUSION ON THE RELEVANT CONSTITUTIONAL QUESTION.

The linchpin of Borman's certiorari Petition is its argument that the court of appeals discarded the district court's findings of fact and made its own findings, allegedly in violation of this Court's prior holdings with respect to Fed. R. Civ. P. 52(a). More specifically, Petitioner's request to this Court to review the court of appeals' decision rests squarely on the notion that the court of appeals was precluded, absent a showing of clear error, from disturbing the district court's conclusion that the Michigan legislature rationally could not have used net worth as a measure of the relative ability to absorb loss. Rule 52(a) is inapplicable here under this Court's prior teachings, and accordingly there is no issue worthy of certiorari.

The Association does not dispute that Rule 52(a) "means what it says." *Bose Corp. v. Consumers Union of United States, Inc.*, 466 U.S. 485, 498 (1984). Under the rule, "findings of fact" made by the district court in an action tried without a jury "shall not be set aside unless clearly erroneous . . . . " It is equally beyond dispute, however, that Rule 52(a) "does not apply to conclusions of law." *Pullman-Standard v. Swint*, 456 U.S. 273, 287 (1982). "Rule 52(a) does not inhibit an appellate court's power to correct errors of law, including those that may

infect a so-called mixed finding of law and fact, or a finding of fact that is predicated on a misunderstanding of the governing rule of law." *Bose Corp., supra* at 501. The district court's legal conclusions, therefore, must be reviewed *de novo* by the appellate court.

The court of appeals held in this case that the district court "exceeded its scope of review" – in other words, erroneously applied the law – "in assessing the constitutionality of § 500.7925(3)" App., p. A-2, and that the district court improperly substituted its judgment for that of the Michigan legislature. *Id.*, p. A-7. This legal conclusion is based on the district court's erroneous attempt to weigh what the court admitted was "conflicting evidence" on the rational relationship issue. As soon as the district court found that the evidence was conflicting (and the court dismissed none of the testimony as incredible), it was bound as a matter of law to conclude that Petitioner had not overcome its heavy burden of proof under the rational basis test. *Minnesota v. Cloverleaf Creamery Co.*, 449 U.S. 456, 464 (1981) (the party challenging the constitutionality of a statute in a rational basis case cannot prevail if the question whether the law is rationally related to a permissible legislative goal is "at least debatable").

This Court has not established a bright-line rule for determining in all instances what is a "finding of fact" and what is a "conclusion of law." *See, Miller v. Fenton*, 474 U.S. 104, 113 (1985).[2] The Court has held, however, in

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[2] This Court's recent decision in *Salve Regina College v. Russell*, ___ U.S. ___, 111 S. Ct. 1217 (1991) is of no help to

(Continued on following page)

instances where so-called "factual findings" really involve the application of legal principles to the particular circumstances of the case and the underlying legal rule becomes meaningful only in the context of those circumstances, that such "findings" must not be subject to the clearly erroneous standard of Rule 52(a). In *Miller v. Fenton*, for example, this Court held that the question whether a confession is voluntary and thus admissible is a question of law that is reviewable *de novo*. The Court reasoned as follows:

> At least in those areas in which Congress has not spoken and in which the issue falls somewhere between a pristine legal standard and a simple historical fact, the fact/law distinction at times has turned on a determination that, as a

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(Continued from previous page)

Petitioner. Contrary to the statement at page 23 of Borman's Petition, the *Salve Regina College* decision did not "[address] the distinction between factual findings and legal conclusions. . . ." Indeed, *Salve Regina College* did not even involve the question whether the lower court properly had applied Fed. R. Civ. P. 52(a).

The issue before the Court in *Salve Regina College* was whether the court of appeals was required to review *de novo* the district court's interpretation of state law or whether a standard of review of such determination similar to Rule 52(a)'s "clearly erroneous" rule should apply. Noting that "[t]he obligation of responsible appellate jurisdiction implies the requisite authority to review independently a lower court's determinations," the Court held that the court of appeals independently should review the district court's determination of state law. 111 S. Ct. at 1221. The Court opined that "[i]ndependent appellate review of legal issues best serves the dual goals of doctrinal coherence and economy of judicial administration." *Ibid.*

> matter of the sound administration of justice, one judicial actor is better positioned than another to decide the issue in question. Where, for example, as with proof of actual malice in First Amendment libel cases, *the relevant legal principle can be given meaning only through its application to the particular circumstances of a case, the Court has been reluctant to give the trier of fact's conclusions presumptive force and, in so doing, strip a federal appellate court of its primary function as an expositor of law.*

474 U.S. at 114 (emphasis supplied). Similarly, in *Bose Corp. v. Consumers Union of United States, Inc., supra,* the Court noted that not all so-called "findings of fact" are subject to review only for clear error. Instead, "findings" which are inextricably tied to the underlying legal rule which gives the findings meaning may be subject to *de novo* review:

> A finding of fact in some cases is inseparable from the principles through which it was deduced. At some point, the reasoning by which a fact is "found" crosses the line between application of those ordinary principles of logic and common experience which are ordinarily entrusted to the finder of fact into the realm of a legal rule upon which the reviewing court must exercise its own independent judgment. Where the line is drawn varies according to the nature of the substantive law at issue. Regarding certain largely factual questions in some areas of the law, the stakes – in terms of impact on future cases and future conduct – are too great to entrust them finally to the judgment of the trier of fact.

466 U.S. at 501, n. 17.

Thus, the district court's "finding" in this case that net worth is not rationally related to a legitimate purpose was freely reviewable by the court of appeals for two reasons. First, the court of appeals was bound to review the finding *de novo* because it is a conclusion on the ultimate *legal* issue in this case – whether any reasonably conceivable state of facts supports the use of net worth as a measure of the relative capacity to absorb loss. Second, the district court's decision was "predicated on a misunderstanding of the governing rule of law." *Bose Corp., supra* at 501. Although the district court found none of the evidence to be incredible, and although the court conceded that the evidence was conflicting, the court nevertheless proceeded to weigh the evidence and decide for itself whether the Michigan legislature *should* have included a net worth cutoff in the Act. Because the district court's "finding" was infected by its error of law, the court of appeals was not required to apply the clearly erroneous standard in Fed. R. Civ. P. 52(a).

Petitioner relies on labels, rather than analysis, to buttress its position that the court of appeals improperly disturbed a "finding of fact." Clearly, however, Petitioner should not be permitted to *call* the district court's determination of the rational relationship issue a "finding of fact" and thereby completely strip the appellate courts of their plenary authority to decide issues of federal law. The court of appeals in this instance did not exceed that authority, and, therefore, Borman's Petition should be denied.

II. THERE IS NO BASIS FOR GRANTING CERTIORARI IN THIS CASE BECAUSE THE COURT OF APPEALS CORRECTLY APPLIED THE SCOPE OF REVIEW REQUIRED BY THIS COURT IN RATIONAL BASIS CASES.

The court of appeals had ample basis in the record to determine that the district court had exceeded the permissible scope of review under the equal protection clause and impermissibly had judged the wisdom of section 7925(3) rather than its rationality. The record before the district court and the court of appeals was replete with evidence of the history and structure of the Act that supports its rationality. Also, the Association called as witnesses at trial qualified experts in accounting, insurance and insurance regulation. All of these witnesses testified that the legislature's use of net worth as an indicator of the relative capacity to absorb loss was rational.

The district court cited this testimony extensively in its opinion, and flatly acknowledged that the evidence on the rationality of the net worth standard was "conflicting." In light of this conflicting credible evidence, the district court was bound under this Court's decisions to undertake no further examination into the Act's rationality. The district court was required at that point to find the Act constitutional and dismiss Petitioner's claim. The district court's failure to do so was an error of law, not fact. The court of appeals merely corrected this error.

A. Under The Rational Basis Test, The District Court Was Not Permitted To Weigh The Admittedly Conflicting Testimony Concerning The Efficacy And Wisdom Of The Legislature's Choices.

This Court has held consistently that review under the Equal Protection Clause's rational basis test is extremely narrow. Under this standard, section 7925(3) is presumed constitutional in the absence of a compelling showing by Petitioner. To satisfy its heavy burden and overcome that presumption, Petitioner was required to negate every reasonably conceivable state of facts justifying the net worth classification. *Minnesota v. Cloverleaf Creamery Co., supra.* In *Cloverleaf Creamery,* this Court stated:

> States are not required to convince the courts of the correctness of their legislative judgments. Rather, 'those challenging the legislative judgment must convince the court that the legislative facts on which the classification is apparently based could not reasonably be conceived to be true by the governmental decisionmaker.' *Vance v. Bradley,* 440 U.S. [93,] 111 [1979]. . . .
>
> Although parties challenging legislation under the Equal Protection Clause may introduce evidence supporting their claim that it is irrational . . . , they cannot prevail so long as 'it is evident from all the considerations presented to [the legislature], and those of which we may take judicial notice, that the question is at least debatable.' [*United States v. Carolene Prods. Co.,* 304 U.S. 144, 153-154 (1938)]. Where there was evidence before the legislature reasonably supporting the classification, litigants may not procure invalidation of the legislation merely by

> tendering evidence that the legislature was mistaken.

449 U.S. at 464.

Moreover, that Petitioner could establish that the net worth standard does not accomplish its intended purpose in all cases – through the use of so-called "typical" examples involving leveraged buyouts and real estate holding companies in which an entity's net worth can change without a corresponding change in its "profitability"[3] – plainly was not enough to overcome Petitioner's heavy burden:

> Even if the classification involved here is to some extent both underinclusive and overinclusive, and hence the line drawn by Congress imperfect, it is nevertheless the rule that in a case like this 'perfection is by no means required.' *Phillips Chemical Co. v. Dumas School Dist.*, 361 U.S. 376, 385 (1960); *accord, San Antonio School Dist. v. Rodriguez*, 411 U.S. 1, 51 (1973). The provision 'does not offend the constitution simply because the classification "is not made with mathematical nicety . . . . "' *Dandridge v. Williams*, 397 U.S. 471, 485 (1970),

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[3] Petitioner's reliance throughout this litigation on these so-called "typical" examples is misleading. There is no evidence in the record or any other reason to believe that any of Petitioner's "typical" situations have any general applicability outside their own specific fact patterns. A "typical" leveraged buyout and a "typical" real estate holding company are not representative of any commercial transaction except for a "typical" leveraged buyout and a "typical" real estate holding company. Petitioner's "typical" examples really are nothing more than examples of some economic situations, but certainly they are not representative of all (nor anything close to a majority of) such situations.

> quoting *Lindsley v. Nat'l Carbonic Gas Co.*, 220 U.S. 61, 78 (1911).

Vance v. Bradley, 440 U.S. 93, 108 (1979) (footnote omitted). A statute does not offend the Constitution merely because it is "unwise or inartfully drawn." *United States R.R. Retirement Bd. v. Fritz*, 449 U.S. 166, 175 (1980). Indeed, the statute may make "rough accommodations – illogical, it may be, and unscientific." *Ibid.*, quoting *Dandridge v. Williams*, 397 U.S. 471, 485 (1970).

Finally, Petitioner's argument that the legislature *could have* measured an insured's relative capacity to absorb loss by using cash flow or liquidity – alone or in conjunction with net worth – or a nebulous term like "financial condition," is not sufficient to establish irrationality under the rational basis test. The many policy choices which the legislature made in establishing the Association and sculpturing the protection it affords, and the wisdom of these choices, are decisions for the legislature to make, not the courts. Where, as the district court found here, the facts supporting the rational relationship are at least debatable, the legislature's judgment must be accepted.

The district court recognized the correct standard, but flat out misapplied it. Based on the record before it, the court of appeals was correct to reverse the district court's judgment.

Petitioner's reliance on *Borden's Farm Prods. Co. v. Baldwin*, 293 U.S. 194 (1934) for the scope of review, and its argument at page 26 of its Petition that the court of appeals violated this Court's holding in *Borden's* by "rel[ying] on conclusions which were not supported by

the facts," miss the mark in at least two significant respects. First, Petitioner misstates the rule in *Borden's*. In that case, the Court was asked to determine the constitutionality under the Equal Protection Clause of legislation which set the wholesale and retail prices of milk sold in New York City by manufacturers with a "well advertised trade name" a minimum of one cent per quart higher than that sold by other manufacturers. In a challenge to the law by a milk producer deemed to have a "well advertised trade name," the trial court – presented only with affidavits and counteraffidavits from both sides – granted the defendant's motion to dismiss Borden' complaint for failure to state a claim.

This Court reversed the trial court's judgment and held that Borden's was entitled to present evidence on its constitutional claims. The Court reaffirmed the settled rule that

> [w]hen the classification make by the legislature is called in question, if any state of facts reasonably can be conceived that would sustain it, there is a presumption of the existence of that state of facts, and one who assails the classification must carry the burden of showing by a resort to common knowledge or other matters which may be judicially noticed, or to other legitimate proof, that the action is arbitrary.

293 U.S. at 209. The Court also held that

> where the legislative action is suitably challenged, and a rational basis for it is predicated upon the particular economic facts of a given trade or industry, which are outside the sphere of judicial notice, these facts are properly the subject of evidence and findings.

Id. at 210.

Borden's thus stands only for the proposition that in a rational basis equal protection case, where the facts supporting the legislative classification cannot be judicially noticed, the party challenging the classification is entitled to an opportunity to overcome its heavy burden of proof by offering evidence in an appropriate proceeding. The Petitioner in *Borden's*, however, never was given a chance to present its evidence to the district court through a trial. This Court thus remanded the *Borden's* case to the district court for further proceedings.

In direct contrast to *Borden's*, Petitioner in the instant case was given the chance to satisfy its burden at trial. Over the course of seven trial days, both sides offered extensive testimony in support of their respective positions. This is all *Borden's* requires, and the court of appeals did nothing in this case to violate the *Borden's* rule.

Second, Petitioner's argument that the court of appeals violated the holding in *Borden's* mischaracterizes the basis for the court of appeals' decision. Although the district court expressly concluded that the evidence on the rational relationship issue was conflicting, that court nevertheless held that Borman's had overcome its heavy burden under the rational basis test. The court of appeals recognized that the district court's holding was a clear misapplication of this Court's rational basis jurisprudence and, supporting its decision with extensive citations to actual testimony in the record, correctly reversed the district court.

B. Credible Evidence Of The History And Structure Of The Act, And The Testimony Of Qualified Experts In Accounting, Insurance And Insurance Regulation Support Its Rationality.

The trial testimony of Elijah Poxson and Dr. George Gottheimer illustrated the reasonably conceivable state of facts connecting net worth and the objectives of the Act which the Michigan legislature could have considered when it adopted the net worth exclusion.

Mr. Poxson was associated with Michigan Mutual Insurance Company, as its general counsel, vice president and then president, from 1959 through 1977. Mr. Poxson's involvement in the legal aspects of the insurance business – including the drafting and monitoring of insurance-related legislation – spans more than 35 years. Tr., 1/13/89, pp. 8-9. Mr. Poxson's testimony was the *only* evidence presented at trial on the history and thinking directly underlying the Michigan Act.

From 1959 through 1974, Mr. Poxson served on the legal committee of the American Mutual Insurance Alliance (the "Alliance"). The Alliance is a trade association of mutual insurance companies interested in all types of issues of importance to the industry. *Id.*, pp. 10-11. Mr. Poxson was an active member of the Alliance's legal committee. *Id.*, p. 11.

Mr. Poxson's testimony confirmed that before the Act was adopted, Michigan insureds (and persons with claims against Michigan insureds) faced with the insolvency of an insurer generally were unprotected from the financial hardships associated with the loss of coverage. Certainly the state provided no such protection. Usually

insureds had no recourse but to stand in line with the remaining unsecured creditors of the insurer and hope to receive a small fraction of the coverage they purchased. *Id.*, p. 19. During the 1960s, a number of insurer insolvencies prompted concern within the Alliance legal committee over the issue of insolvency and, more specifically, over measures which were being considered to address the problem. *Id.*, p. 13.

In the late 1960s, Senator Magnuson proposed legislation in the United States Congress to create a national, pre-insolvency-funded insurance pool to pay covered claims of insureds whose carriers had become insolvent (which would operate much as the FDIC operates with respect to insured banks). *Id.*, p. 20. The pendency of the Magnuson bill prompted the Alliance legal committee to form a subcommittee of three members, including Mr. Poxson, to focus specifically on the issue of guaranty fund legislation. *Ibid.* The result of the subcommittee's discussions was the drafting of a model guaranty association bill in late 1968. The model bill proposed a post-insolvency fund to be administered by the states – which already actively regulated insurance companies – rather than the federal government. *Id.*, pp. 20-21.

In early 1969 the Michigan Insurance Commissioner, which was and is charged by state statute with the enforcement of Michigan's insurance laws and the regulation of the insurance industry in the state, appointed Mr. Poxson to a committee of general counsel from several insurance companies which the Commissioner had formed to address the insolvency issue in Michigan. The Commissioner appointed an actuary from the Michigan Insurance Bureau to chair the committee. The committee

focused at that time on a guaranty fund bill that was pending in the Michigan legislature. *Id.*, pp. 21-23.

The Commissioner's committee studied the pending legislation and concluded that it did not adequately address the problems raised by insurer insolvency. *Id.*, p. 22. The committee considered the Alliance model bill, concluded that it was a better solution to the insolvency problem than the pending legislation, and submitted it as a substitute for the bill then under consideration by the legislature. *Id.*, p. 25. On August 11, 1969, the substitute bill became the Michigan Property & Casualty Guaranty Act.

Mr. Poxson, who drafted the Alliance model bill and was involved with its consideration through the time it was submitted as a substitute bill, explained the development and rationale behind the net worth limitation in the Act:

> Q: Now, could you tell the Court what your rationale was, as one of the co-authors of this bill, for that provision?
>
> A: . . . . I believe that anyone, any person or corporation which had a networth [sic] of a million dollars,[4] in other words the difference between assets minus liabilities, was a person of

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[4] The Alliance model bill contained a flat $1 million net worth cap. The Act as passed indexes the cap so that it fluctuates as inflation affects premium writings in Michigan. The Commissioner's committee found (and subsequent history has confirmed) that the indexing approach is more equitable than a flat $1 million cutoff. Tr., 1/13/89, pp. 49-50.

> substantial wealth and, therefore, would be able to bear a reasonably large, unexpected loss without too much difficulty, even if they were uninsured.

Id., pp. 44-45.

Mr. Poxson testified that in considering how to limit eligibility for the limited coverage to be provided under the Act, the Commissioner's committee considered other measurers of wealth, such as assets, in addition to net worth. *Id.*, pp. 48, 66. The drafters of the Alliance model bill and the Insurance Commissioner's committee rejected the use of assets, however, and decided on net worth. Mr. Poxson testified that the members of the Commissioner's committee felt the use of assets as a measure of one's relative capacity to absorb loss, without also considering corresponding liabilities, was "not representative of a person's ability to respond." *Id.*, p. 66.

In addition to Mr. Poxson, Dr. George Gottheimer, whose academic, professional and teaching experience in such areas as reinsurance and insolvency span 35 years, testified about the concerns in the insurance industry and in state legislatures over the past 20 to 25 years which led to the enactment of guaranty association statutes and the inclusion of net worth provisions. Dr. Gottheimer's undisputed testimony confirmed that the chief concerns of legislators and regulators in the late 1960s, when the Act was passed, and in the early to mid 1980s when several other states enacted guaranty fund legislation with net worth exclusions, were (1) what could be done to protect, at least in part, those in society who are hardest hit by the insolvency of their insurers and (2) given the conceded limits on financial resources, how

those resources should be allocated so they reach those most in need of them. *Id.*, pp. 96, 109.

Dr. Gottheimer opined that, given these concerns, using net worth as a measure of an insured's cushion to absorb unforeseen losses was and is rationally related to the purposes underlying the Act. Tr., 1/17/89, pp. 8, 10.

The testimony of Julius Otten, a partner in the public accounting firm of KPMG Peat Marwick, and an accountant with over 25 years experience dealing with insurance-related issues from an accounting standpoint, also supported the net worth classification. Mr. Otten testified that using net worth as an indicator of financial wealth and the relative capacity to absorb losses is indeed rational:

> I think you can characterize networth [sic] as a – as a cushion, which can be used to absorb losses. Those losses can come from operations. They can come from contingencies, which can't be anticipated but materialize – maybe materialize over time. Certainly within the insurance industry itself, particularly the casualty industry, surplus or networth [sic], if you will, is perceived to be the cushion to absorb adverse losses. . . .

Tr., 1/18/89, p. 17.

Mr. Otten vigorously disagreed with assertions made by Robert Epstein, Borman's general counsel, that there is

no relationship between net worth and the capacity to absorb loss:[5]

> While I could agree different parties might perceive the relationship to vary, there is certainly some relationship at a minimum between net-worth [sic] and the capacity to absorb loss.

Id., p. 10.

Mr. Otten testified that net worth is by itself a useful (though imperfect) indicator of a person's relative capacity to absorb losses. Mr. Otten testified that given this usefulness, it certainly is rational for Michigan's legislature to look at an insured's net worth when seeking to allocate insolvency losses to those best able to absorb them. *Id.*, pp. 10-11. Additionally, Mr. Otten testified that while the legislature could have defined the cutoff by using other indicia of financial condition, such as assets, cash flow or liquidity, none of these measures would be as equitable or administratively workable as net worth. *Id.*, p. 11.[6]

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[5] Indeed, Mr. Epstein's assertion was refuted by the Petitioner's own accounting expert, David Simmons, who conceded on cross examination that net worth does provide at least "information" about an insured's financial condition and its ability to absorb an unexpected loss. Tr., 1/11/89, p. 41.

[6] Contrary to the argument at page 28 of the Petition, the court of appeals did not hold that administrative ease is itself sufficient to support the Act's constitutionality. Quite to the contrary, the court of appeals held, consistent with this Court's past decisions, that the legislature may consider such efficiencies when deciding between two reasonable alternatives. Having decided that under the rational basis test the Act was not irrational, the court of appeals' discussion of the superior administrative workability of the net worth standard as opposed to other reasonable eligibility standards was entirely proper.

Petitioner's general counsel, Robert Epstein, and its accounting expert, David Simmons, agreed on cross examination with Mr. Otten's testimony that, although the truest measure of an insured's ability to withstand unexpected casualty losses is its entire "financial condition," net worth does in fact provide information that can be used to assess financial condition and the relative capacity of an insured to absorb an unexpected loss. Tr., 1/9/89, p. 87; Tr., 1/11/89, p. 41. Neither witness expressed an opinion on the administrative workability of a guaranty fund statute which based eligibility for coverage on an insured's "financial condition."

Jean Carlson, Deputy Commissioner of Insurance for Policy and Compliance in Michigan, also testified in favor of the rationality of the net worth exclusion. Ms. Carlson's testimony is based on her experience and educational background in insurance regulation, economics and public policy issues related to the regulation of the insurance industry in Michigan. Ms. Carlson testified that, faced with the tough policy choices involved in establishing a guaranty fund with limited resources to alleviate some of the financial hardships resulting from insolvency, it was rational for the legislature to use net worth as a means of allocating resources to those most in need of them:

> I think, speaking as an economist and not as an accountant, that I don't know how else I would measure wealth for most people, whether [sic] other than networth [sic]. You know, assets less whatever liabilities or other amounts are owed

> leaves you basically what your – the assets that are left are the ones no one else has a claim against. . . .

Tr., 1/17/89, p. 98.

The evidence offered at trial by the Association's witnesses clearly established that net worth is a good and rational indicator of an insured's (and an insurer's) relative capacity to absorb loss. Indeed, Borman's own witnesses admitted that net worth does provide information about the relative capacity to handle unexpected and uninsured losses. Tr., 1/9/89, p. 87; Tr., 1/11/89, p. 41.

With this substantial body of evidence in front of it, the district court was required to find that Petitioner had not satisfied its burden under the rational basis standard, and that section 7925(3) is constitutional. Its failure to do so was a clear error of law which the court of appeals properly corrected. Petitioner has no basis for further review of that judgment by this Court.

CONCLUSION

For the foregoing reasons, the Petition for a writ of certiorari should be denied.

Respectfully submitted,

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